Supreme Court, U.S.
FILED
(1)
No. 04-664 NOV 15 2004
OFFICE OF THE CLERK

In The

Supreme Court of the United States

LOOP CORP.; LEON GREENBLATT; NOLA, LLC; REPURCHASE CORP.; LESLIE JABINE; TELETECH SYSTEMS, INC.; CHIPLEASE, INC.; AND BANCO PANAMERICANO, INC.,

Petitioners,

v.

U.S. TRUSTEE,

Respondent.

On Petition For A Writ Of Certiorari To The United States Court Of Appeals For The Eighth Circuit

PETITION FOR A WRIT OF CERTIORARI

ROBERT M. FISHMAN
PETER J. ROBERTS
Counsel Of Record
BRIAN L. SHAW
SHAW GUSSIS FISHMAN GLANTZ WOLFSON & TOWBIN LLC
321 North Clark Street, Suite 800
Chicago, Illinois 60610
(312) 541-0151

Attorneys for Petitioners

COCKLE LAW BRIEF PRINTING CO. (800) 225-6964
OR CALL COLLECT (402) 342-2831

QUESTIONS PRESENTED

Should the Court grant certiorari to resolve a split among circuits as to whether a court has discretion to neither convert nor dismiss a bankruptcy case under chapter 11 of the U.S. Bankruptcy Code when cause exists to do so under 11 U.S.C. § 1112(b)?

Did the U.S. Court of Appeals for the Eighth Circuit misinterpret 11 U.S.C. § 1112(b) when it held that a court had discretion to neither dismiss nor convert a case under chapter 11 of the U.S. Bankruptcy Code when cause existed to do so under 11 U.S.C. § 1112(b)?

Did the lower courts' rulings create a *per se* rule that cases under chapter 11 of the U.S. Bankruptcy Code that involve a liquidating debtor always meet the cause standard set forth under 11 U.S.C. § 1112(b)(1), effectively removing liquidating chapter 11 bankruptcy cases from the U.S. Bankruptcy Code despite the express allowance for such cases under other sections of the U.S. Bankruptcy Code?

RULE 29.6 STATEMENT AND PARTIES TO THE CASE

Petitioners are Loop Corp.; Leon Greenblatt; Nola, LLC; Repurchase Corp.; Leslie Jabine; Teletech Systems, Inc.; Chiplease, Inc.; and Banco Panamericano, Inc. Respondent is the U.S. Trustee. In addition, Health Risk Management, Inc. and its affiliated debtors and the Official Committee of Unsecured Creditors were parties to the proceedings below.

Pursuant to S. Ct. Rule 29.6, petitioners state that there is no parent of any of the Petitioners and no public company owns the stock of any of the Petitioners.

TABLE OF CONTENTS

	Page
QUESTIONS PRESENTED	i
RULE 29.6 STATEMENT AND PARTIES TO THE CASE	ii
TABLE OF CONTENTS	iii
TABLE OF AUTHORITIES	iv
PETITION FOR A WRIT OF CERTIORARI	1
OPINIONS BELOW	1
JURISDICTION	1
RELEVANT STATUTORY PROVISIONS	2
STATEMENT	3
REASONS FOR GRANTING THE PETITION	7
REVIEW IS WARRANTED BECAUSE TWO COURTS OF APPEALS ARE SPLIT ON THE ISSUE OF WHETHER A COURT HAS THE DISCRETION TO ELECT TO NEITHER DISMISS NOR CONVERT A CHAPTER 11 BANKRUPTCY CASE ONCE CAUSE HAS BEEN FOUND EXIST, AND THIS SPLIT IS IRRECONCILABLE	8
THE EIGHTH CIRCUIT'S POSITION IS INCORRECT	9
A. Once Cause Has Been Found, Discretion Is Limited to Conversion or Dismissal	9
B. The Eighth Circuit's Application Of Cause Under § 1112(B) Is Incorrect And Results In A Per Se Rule Against Liquidating Chapter 11 Cases.	11
CONCLUSION	15
TABLE OF APPENDICES	i

TABLE OF AUTHORITIES

Page

CASES

AMC Mortgage Co., Inc. v. Tenn. Dep't of Revenue (In re AMC Mortgage Co., Inc.), 213 F.3d 917 (6th Cir. 2000) 9

Camden Ordnance Mfg. Co. of Ark., Inc. v. U.S. Tr. (In re Camden Ordnance Mfg. Co. of Ark., Inc.), 245 B.R. 794 (E.D. Pa. 2000) 9

In re All Am. of Ashburn, Inc., 40 B.R. 104 (Bankr. N.D. Ga. 1984) 12

In re Alves Photo Serv., Inc., 6 B.R. 690 (Bankr. D. Mass. 1980) 12

In re Econ. Cab & Tool Co., Inc., 44 B.R. 721 (Bankr. D. Minn. 1984) 11, 12

In re Gonic Realty Trust, 909 F.2d 624 (1st Cir 1990) 11

In re Schriock Constr., Inc., 167 B.R. 569 (Bankr. D. N.D. 1994) 10, 11

In re Shockley, 197 B.R. 677 (Bankr. D. Mont. 1996) ... 9, 11

In re The Adbrite Corp., 290 B.R. 209 (Bankr. S.D.N.Y. 2003) 12

In re W. Pac. Airlines, Inc., 218 B.R. 590 (Bankr. D. Col. 1998) 12

Rollex Corp. v. Associated Materials, Inc. (In re Superior Siding & Window Inc.), 14 F.3d 240 (4th Cir. 1994) 8, 11

U.S. Tr. v. GPA Technical Consultants, Inc. (In re GPA Technical Consultants, Inc.), 106 B.R. 139 (Bankr. S.D. Ohio 1989) 13

TABLE OF AUTHORITIES – Continued

Page

STATUTES

11 U.S.C. § 102 10

11 U.S.C. § 1112 ..... *passim*

11 U.S.C. § 1123 ..... 3, 7, 13

28 U.S.C. § 1254 1

OTHER AUTHORITIES

H.R. No. 95-595, 95th Cong., 1st Sess. 405 (1977) 10

S.R. No. 95-989, 95th Cong., 2nd Sess. 117 (1978) 10

PETITION FOR A WRIT OF CERTIORARI

Petitioners Loop Corp.; Leon Greenblatt; Nola, LLC; Repurchase Corp.; Leslie Jabine; Teletech Systems, Inc.; Chiplease, Inc.; and Banco Panamericano, Inc. (collectively, "Petitioners") respectfully petition for a writ of certiorari to review the judgment of the U.S. States Court of Appeals for the Eighth Circuit ("Eighth Circuit") in this case.

OPINIONS BELOW

The opinion of the Eighth Circuit is reported at 379 F.3d 511 (8th Cir. 2004) and reprinted in the appendix hereto ("App.") 1. The opinion of the U.S. District Court for the District of Minnesota ("District Court") is published at 290 B.R. 108 (Bankr. D. Minn. 2003) and reprinted at App. 16. The order of the U.S. Bankruptcy Court for the District of Minnesota ("Bankruptcy Court") is not reported and is reprinted at App. 30.

JURISDICTION

The Eighth Circuit entered its opinion and judgment on August 16, 2004. This petition for a writ of certiorari has been filed within ninety days of such opinion and judgment. This Court has jurisdiction over this case pursuant to 28 U.S.C. § 1254(1).

RELEVANT STATUTORY PROVISIONS

Section 1112(b) of the Bankruptcy Code[1] provides in relevant part:

> (b) Except as provided in subsection (c) of this section, on a request of a party in interest or the United States trustee or bankruptcy administrator, and after notice and a hearing, the court may convert a case under this chapter to a case under chapter 7 of this title or may dismiss a case under this chapter, whichever is in the best interests of creditors and the estate, for cause, including –
>
> (1) continuing loss to or diminution of the estate and absence of a reasonable likelihood of rehabilitation;

11 U.S.C. § 1112(b).

Section 1123 provides in relevant part:

> (a) Notwithstanding any otherwise applicable nonbankruptcy law, a plan shall –
>
> * * *
>
> (5) provide adequate means for the plan's implementation such as –
>
> * * *
>
> (D) sale of all or any part of the property of the estate, either subject to or free of any lien, or the distribution of all or any part of

[1] Unless otherwise indicated, all statutory references relate to the U.S. Bankruptcy Code, 11 U.S.C. §§ 101 *et seq.* (2004).

the property of the estate among those having an interest in such property of the estate;

* * *

(b) Subject to subsection (a) of this section, a plan may –

* * *

(4) provide for the sale of all or substantially all of the property of the estate, and the distribution of the proceeds of such sale among the holder of claims or interests.

11 U.S.C. § 1123.

STATEMENT

The questions presented arise out of the bankruptcy cases of Health Risk Management, Inc. and its affiliated debtors (collectively, "Debtors"), Case Nos. 01-43354, 01-43355, 01-43356 and 01-43357 (collectively, "Case"), filed in the Bankruptcy Court. The Debtors filed their voluntary petitions on August 7, 2001. In the first three months of the Case, the Debtors were able to successfully market their businesses and sell their assets primarily as going concerns.

The Debtors filed their initial plan of reorganization on December 5, 2001. At that time, and through January 10, 2002, the Debtors' principal remaining assets consisted of: (a) a potential cause of action against Ernst & Young arising out of its provision of auditing and actuarial services to the Debtors; (b) potential causes of action against former insiders of the Debtors, some of whom

served on the Official Committee of Unsecured Creditors ("Committee") in this Case; (c) preference actions under § 547; and (d) net operating losses ("NOLs") with an estimated value in terms of income taxes sheltered of approximately $10 million to $20 million. The NOLs would have no value if the Debtors are liquidated under chapter 7 of the Bankruptcy Code.

On January 10, 2002, the U.S. Trustee ("UST") filed her Motion to Dismiss or Convert ("UST Motion to Convert"), which sought conversion or dismissal of the Case under § 1112(b)(1), (2) and/or (3). A hearing on the UST Motion to Convert was held on February 6, 2002. (App. 31.) Admittedly, the UST neither submitted nor presented any evidence in support of its Motion to Convert. (App. 35.) Rather, the UST relied on the record of the Case.

At the conclusion of the February 6, 2002 hearing, the Bankruptcy Court held as a matter of law that under § 1112(b)(1), (a) "rehabilitation . . . means a rehabilitation of the debtor and its business" (App. 40-41), and (b) the costs of administration of a liquidating estate constitute diminution of the estate for purposes of conversion under § 1112(b)(1). (App. 40.) The Bankruptcy Court also found that (c) the confirmation process would cause professional expenses to be incurred with no guaranty of confirmation (App. 38); (b) the plan seems "at least unduly complicated" for a case of this size (App. 39); (c) it was "unconvinced at all that either the costs or delay would be any more substantial in a Chapter 7 case than they would be in a Chapter 11 case" (App. 40); (d) "[n]o rehabilitation is proposed here" (App. 41); and (e) "administrative expenses are running" (App. 40.) The Bankruptcy Court then held that the UST had shown cause for conversion under

§ 1112(b)(1), but continued the matter until March 13, 2002 for the parties to negotiate a consensual plan. (App. 41-42, 48.)

The Debtors, the Petitioners and the Committee were unable to negotiate a consensual plan, and, on March 4, 2002, the Committee filed its own Motion to Convert or Dismiss ("Committee Motion to Convert"), on which it sought an expedited hearing on March 7, 2002. The Bankruptcy Court refused the Committee's request for an expedited hearing on its Motion and continued the matter until March 13, 2002. (App. 44-45.)

On March 13, 2002, the Debtors filed an amended plan of reorganization. Also on March 13, 2002, the Bankruptcy Court held the continued hearing on the UST Motion to Convert. (App. 46-47.) The Bankruptcy Court concluded the hearing without making any additional findings of fact or conclusions of law. (App. 48-49.) Rather, the Bankruptcy Court incorporated its February 6, 2002 conclusions and findings and converted the Case for cause shown under § 1112(b)(1) because the "terms of the – on which I continued the hearing have not been met and so I'm going to grant the motions and convert the cases to Chapter 7." *Id.* The Bankruptcy Court also summarily noted that the Committee "seems to me [to be] the representative body here to make the determination about what is best for unsecured creditors." (App. 49.)

On March 22, 2002, Appellants filed their Notice of Appeal to the District Court. On February 5, 2003, the District Court entered its Memorandum Opinion affirming the Bankruptcy Court's March 13, 2001 order for the reasons stated therein. (App. 16-29.) On March 7, 2003, Petitioners filed their Notice of Appeal with the Eighth

Circuit. Argument was heard on February 13, 2004, and the Eighth Circuit affirmed the lower courts' decisions on August 16, 2004. (App. 1.)

In reaching its decision, the Eighth Circuit held that ongoing administrative expenses of a liquidating chapter 11 case, alone, constitute diminution of the estate under § 1112(b)(1), and that the lower courts correctly interpreted the term "rehabilitation" to require an operating business. (App. 6-8.) As such, the Eighth Circuit held that the lower courts properly found that cause existed under § 1112(b)(1) to convert or dismiss the Cases. *Id.*

At the same time, the Eighth Circuit also acknowledged that under its interpretation it is hard to envision a liquidating chapter 11 case where cause would not exist to convert or dismiss a case under § 1112(b)(1) and noted its sensitivity to the Petitioners' concerns. (App. 8.) The Eighth Circuit then attempted to reconcile its concern by holding that § 1112(b)(1) provided the court discretion to elect neither to convert nor dismiss a chapter 11 case even if there was a showing of cause. *Id.*

As explained below, however, the Eighth Circuit's decision that a court still has discretion to elect neither to convert nor dismiss a chapter 11 case once cause is shown under § 1112(b) is both wrong and in conflict with decisions of other circuit courts of appeal. In addition, the Eighth Circuit's erroneous conclusion tarnishes its affirmation that cause existed in the Case to convert or dismiss under § 1112(b)(1) because, as the Eighth Circuit acknowledged, the factors that the lower courts equated to cause are present in every liquidating chapter 11 case. Thus, if such factors really constitute cause under § 1112(b)(1) (thus mandating conversion or dismissal under the proper

interpretation of § 1112(b)), liquidating chapter 11 cases are effectively written out of the Bankruptcy Code. It is this result that is in conflict with other sections of the Bankruptcy Code, such as § 1123, that clearly allow debtors to liquidate their bankruptcy estates under chapter 11 of the Bankruptcy Code. 11 U.S.C. § 1123.

REASONS FOR GRANTING THE PETITION

Currently, there is a split among circuit courts of appeal on the issue of whether a bankruptcy court has discretion to elect to neither dismiss nor convert a chapter 11 case once cause has been found to exist under § 1112(b), or, on the other hand, whether the bankruptcy court may only choose to either dismiss or convert the case once cause has been found. 11 U.S.C. § 1112(b). This split is significant. If a bankruptcy court must elect to dismiss or convert a case when there is a showing of cause, as the U.S. Court of Appeals for the Fourth Circuit ("Fourth Circuit") has ruled, then the Eighth Circuit's interpretation that cause always exists under § 1112(b)(1) effectively removes liquidating bankruptcy cases from chapter 11 of the Bankruptcy Code. This position, which in essence is a *per se* rule that cause exists to dismiss or convert to chapter 7 every liquidating chapter 11 case, would conflict with other Bankruptcy Code sections that expressly allow a debtor to liquidate all of its assets under chapter 11 of the Bankruptcy Code. *See, e.g.*, 11 U.S.C. § 1123. Finally, as also explained below, the Eighth Circuit's decision that a court's discretion under § 1112(b) includes the discretion to allow a bankruptcy case to remain in chapter 11, is also wrong and a misinterpretation of § 1112(b). 11 U.S.C. § 1112(b).

REVIEW IS WARRANTED BECAUSE TWO COURTS OF APPEALS ARE SPLIT ON THE ISSUE OF WHETHER A COURT HAS THE DISCRETION TO ELECT TO NEITHER DISMISS NOR CONVERT A CHAPTER 11 BANKRUPTCY CASE ONCE CAUSE HAS BEEN FOUND EXIST, AND THIS SPLIT IS IRRECONCILABLE

As noted above, the Eighth Circuit reconciled its belief that the Bankruptcy Court's interpretation of what constitutes cause under § 1112(b)(1) does not create a *per se* rule that liquidating chapter 11 cases must be converted or dismissed by holding that once cause is found to exist, the court still has discretion to elect not to dismiss or convert the bankruptcy case. (App. 8.) The Eighth Circuit's holding, however, directly contradicts the holding of the Fourth Circuit in *Superior Siding. Rollex Corp. v. Associated Materials, Inc. (In re Superior Siding & Window Inc.)*, 14 F.3d 240, 242 (4th Cir. 1994).

In *Superior Siding,* the Fourth Circuit was faced with the question of whether a lower court properly dismissed, rather than converted to chapter 7, a chapter 11 case found to have been filed in bad faith. *Id.* The Fourth Circuit first noted that the cause requirement of § 1112(b) had been met with a finding of subjective bad faith on the part of the debtor. *Id.* The Fourth Circuit then held that since cause had been shown, the lower court next had to consider the best interests of all creditors and the estate before determining whether it was more appropriate to convert or more appropriate to dismiss the bankruptcy case. *Id* at 242-543 ("[o]nce 'cause' is established, a court is required to consider this second question of whether to dismiss or convert," which requires the court to "ascertain

the impact on the creditors and on the estate of each of the options").

The Fourth Circuit's position that once cause has been found to exist under § 1112(b), a court has discretion only to decide whether conversion or dismissal in the best interests of the creditors and the estate is in direct conflict with the Eighth Circuit's decision. The Eighth Circuit held that a court's discretion in such a situation may also allow for the case to remain in chapter 11. Therefore, there exists a conflict among circuits that is central to the interpretation and application of § 1112(b), and which can only be resolved by this Court.

THE EIGHTH CIRCUIT'S POSITION IS INCORRECT

A. Once Cause Has Been Found, Discretion Is Limited to Conversion or Dismissal.

It is without question that a court has broad discretion when evaluating whether cause exists to convert or dismiss a chapter 11 case under § 1112(b). *AMC Mortgage Co., Inc. v. Tenn. Dep't of Revenue (In re AMC Mortgage Co., Inc.)*, 213 F.3d 917, 920 (6th Cir. 2000). In addition, once a court has exercised such discretion, it continues to have broad discretion to determine whether the option of dismissal or the option of conversion to chapter 7 is best for unsecured creditors and the estate. *Superior Siding*, 14 F.3d at 242. However, this discretion is not without boundaries. Rather, the court is limited by the two statutory options before it, and cannot choose to do nothing. *Id; Camden Ordnance Mfg. Co. of Ark., Inc. v. U.S. Tr. (In re Camden Ordnance Mfg. Co. of Ark., Inc.)*, 245 B.R. 794, 798 (E.D. Pa. 2000); *In re Shockley*, 197 B.R. 677, 680

(Bankr. D. Mont. 1996); *In re Schriock Constr., Inc.*, 167 B.R. 569, 574 (Bankr. D. N.D. 1994).

The limitation of having the discretion to choose only between dismissal or conversion is supported by the statutory language of § 1112(b), the majority of case law on the issue and common sense. The plain language of § 1112(b) expressly gives a court two options if it finds "cause": "the court may convert a case under this chapter to a case under chapter 7 of this title or may dismiss a case under this chapter, whichever is in the best interest of creditors and the estate." 11 U.S.C. § 1112(b). Nowhere does the statute set out the third option chosen by the Eighth Circuit, allowing the case to remain under chapter 11, or indicate that the two mentioned options are non-exclusive. *Id.* In contrast, when setting forth the many bases that constitute cause under § 1112(b), the statutory language makes it clear that the list is meant to be non-exclusive, introducing it with the word "including." *Id.*; 11 U.S.C. § 102(3).

Both of these plain language interpretations are supported by the legislative history behind § 1112(b), which provides:

> Subsection (b) gives wide discretion to the court to make an appropriate disposition of the case when a party in interest requests. The court is permitted to convert a reorganization case to a liquidation case or to dismiss the case, whichever is in the best interests of creditors and the estate, only for cause.

H.R. No. 95-595, 95th Cong., 1st Sess. 405 (1977); S.R. No. 95-989, 95th Cong., 2nd Sess. 117 (1978). In addition, this limitation on a court's discretion is supported by numerous

other court decisions. *See, e.g., Superior Siding*, 14 F.3d at 242; *Camden Ordnance*, 245 B.R. at 798; *Shockley*, 197 B.R. at 680; *Schriock Constr.*, 167 B.R. at 574.

Finally, common sense also supports the position set forth by the Fourth Circuit in *Superior Siding*. As noted above, a court has broad discretion to determine that cause exists under § 1112(b) to convert or dismiss a chapter 11 case. "Cause" may be evidenced by many different factors, both enumerated and not enumerated in the statute. *In re Gonic Realty Trust*, 909 F.2d 624, 626 (1st Cir 1990). However, it makes no sense that given such broad discretion, a court would first determine that cause exists to convert or dismiss a chapter 11 case, and then exercise additional discretion to do neither. For these reasons, the decision of the Eighth Circuit contradicts § 1112(b) and should be reviewed by this Court.

B. The Eighth Circuit's Application Of Cause Under § 1112(b) Is Incorrect And Results In A Per Se Rule Against Liquidating Chapter 11 Cases.

"To show cause under Section 1112(b)(1), a moving party must demonstrate that there is both a continuing loss to or diminution of the estate *and* absence of a reasonable likelihood of rehabilitation." *In re Econ. Cab & Tool Co., Inc.*, 44 B.R. 721, 724 (Bankr. D. Minn. 1984) (emphasis in original). "To determine whether a moving party has proved continuing loss to or diminution of the estate, the Court must look beyond the bare form of the debtor's filed reports and the form of its financial statements." *Id.* In the context of a liquidating chapter 11 case, the inquiry into loss to or diminution of the estate should not end with the inevitable negative cash flow incurred by

a company that has liquidated its hard assets and is now pursuing causes of action on its own. *In re W. Pac. Airlines, Inc.*, 218 B.R. 590, 594-95 (Bankr. D. Col. 1998); *see also In re All Am. of Ashburn, Inc.*, 40 B.R. 104, 108 (Bankr. N.D. Ga. 1984) (holding that in a liquidating chapter 11 case the relevant inquiry under § 1112(b) is whether the administrative expenses will be less of a burden under chapter 7 than under chapter 11); *In re Alves Photo Serv., Inc.*, 6 B.R. 690, 693 (Bankr. D. Mass. 1980).

Moreover, "the term 'rehabilitation' does not mean the same thing as reorganization, as such term is used in Chapter 11. The preferred interpretation of the term as used in Section 1112(b)(1) refers to the ability to confirm a plan of reorganization, which may provide for liquidation and is considerably different from obtaining a sound financial structure." *Alves Photo*, 6 B.R. at 693 (citing COLLIER ON BANKRUPTCY, ¶ 1112.03 at 1112 (15th ed. 1980)); *see also Econ. Cab*, 44 B.R. at 725, n.2; *In re The Adbrite Corp.*, 290 B.R. 209, 216 (Bankr. S.D.N.Y. 2003) ("rehabilitation does not mean the same thing as reorganization for purposes of Chapter 11 because a reorganization may include an orderly or complete liquidation").

Despite the liquidating posture of the Case, the lower courts incorrectly held that as a matter of law the legal standard under § 1112(b)(1) was met because (a) diminution under § 1112(b)(1) occurs when a debtor has liquidated its assets and is now incurring costs related to completing the administration of its estate (App. 33), and (b) rehabilitation requires "getting businesses up and going and running again" not "sucking all the assets out and giving them away." (App. 34.) However, the lower courts were incorrect, as they failed to properly apply

§ 1112(b)(1) within the context of a *liquidating* chapter 11 case.

Instead, in contravention of both the Bankruptcy Code and established case law, the legal standard enunciated by each of the lower courts creates a *per se* rule that cause exists under § 1112(b) in all liquidating chapter 11 cases. *See, e.g.*, 11 U.S.C. § 1123(a)(5)(D) and (b)(4); *U.S. Tr. v. GPA Technical Consultants, Inc. (In re GPA Technical Consultants, Inc.)*, 106 B.R. 139, 142 (Bankr. S.D. Ohio 1989) (noting that "[l]iquidating plans are contemplated under the Bankruptcy Code" and holding that the "probability that a liquidating plan may be filed thus does not serve as a ground for conversion or dismissal because the submission of such a plan is proper under Chapter 11") (citing *In re Denrose Diamond*, 49 B.R. 754, 756 (Bankr. S.D.N.Y. 1985)) and cases cited therein.

As actually acknowledged by the Eighth Circuit, the result of this interpretation of the legal standard of cause under § 1112(b)(1) is that every liquidating chapter 11 case, by definition, will ultimately come to a point where it must be converted or dismissed for cause. (App. 8.) This is so because once a liquidating debtor's business operations are sold, it no longer generates regular operational cash flow. Instead, it waits for cash flow from the liquidation of it remaining assets, many of which are intangible such as lawsuits, and many of which require an initial outlay of cash to have any chance to achieve an end game, positive recovery. Therefore, when any particular time is looked at in a vacuum, a liquidating debtor may very well have negative cash flow, whether from an initial outlay spoken of above, or simply from the costs of administration (both of which, ironically, would exist at a similar level in a liquidation conducted under chapter 7).

However, that time in a vacuum may be misleading if taken separate and apart from the overall results of a liquidating debtor's cash flow in chapter 11.

Moreover, every liquidating chapter 11 debtor ultimately liquidates all of its assets, thereby leaving the costs of administration and distribution to creditors to "suck" the fruits of that liquidation out of the estate. Obviously, there would be no chance for the debtor to "rehabilitate" in a chapter 11 liquidation as that term was interpreted by the lower courts.

The effect of the creation of this *per se* rule, which was also implicitly acknowledged by the District Court, was reconciled by the Eighth Circuit with its second incorrect interpretation of §1112(b), that a court has the discretion to elect neither to dismiss nor convert a bankruptcy case after it has found that cause exists to do so under § 1112(b). On the other hand, the District Court justified its affirmation of the *per se* standard by noting that the bankruptcy court still has broad discretion, conveniently ignoring the fact that by definition, the existence of a *per se* rule precludes discretion. (App. 24-26.)

The Eighth Circuit's affirmation of the incorrect application of cause under §1112(b)(1) in a liquidating chapter 11 case, which could effectively result in the preclusion of liquidating chapter 11 cases, not only conflicts with the language of the statute itself, it conflicts with the Bankruptcy Code and established case law. For this reason as well, the decision of the Eighth Circuit should be reviewed by this Court.

CONCLUSION

For these reasons, Petitioners respectfully request that the Court issue a writ of certiorari to review the decision of the Eighth Circuit in this Case.

Respectfully submitted,

Dated: November 15, 2004

Robert M. Fishman
Peter J. Roberts
Counsel of Record
Brian L. Shaw
Shaw Gussis Fishman Glantz
Wolfson & Towbin LLC
321 North Clark Street,
Suite 800
Chicago, Illinois 60610
(312) 541-0151

TABLE OF APPENDICES

Opinion of the U.S. Court of Appeals for the Eighth Circuit decided August 16, 2004 (*Loop Corp.*, 379 F.3d 511 (8th Cir. 2004)) ..... App. 1

Opinion of the U.S. District Court for the District of Minnesota (*Loop Corp. v. U.S Tr.*, 290 B.R. 108 (Bankr. D. Minn. 2003)) ..... App. 16

Order of U.S. Bankruptcy Court, District of Minnesota Converting Cases to Cases Under Chapter 7 Dated March 14, 2002 ..... App. 30

Excerpts from Transcript of Proceedings Dated February 6, 2002 ..... App. 31

Excerpts from Transcript of Proceedings Dated March 7, 2002 ..... App. 43

Excerpts from Transcript of Proceedings Dated March 13, 2002 ..... App. 46

379 F.3d 511

LOOP CORP.; Leon Greenblatt; Nola, LLC; Repurchase Corp.; Leslie Jabine; Teletech Systems, Inc.; Chiplease, Inc.; Banco Panamericano, Creditors-Appellants,

v.

UNITED STATES TRUSTEE; Committee of Unsecured Creditors, Movants Below-Appellees.

No. 03-1786.

United States Court of Appeals,
Eighth Circuit.

Submitted: Feb. 13, 2004.

Filed: Aug. 16, 2004.

Brian L. Shaw (argued), Chicago, IL (Jane S. Welch and Daniel J. McGarry, Minneapolis, MN; and Robert M. Fishman and Allen J. Guon, Chicago, IL), for appellant.

Michael R. Fadlovich (argued), U.S. Trustee's Office, Minneapolis, MN, for appellee.

Before MORRIS SHEPPARD ARNOLD, JOHN R. GIBSON, and RILEY, Circuit Judges.

JOHN R. GIBSON, Circuit Judge.

The district court affirmed the bankruptcy court's Order of Conversion of the debtors' Chapter 11 case to a case under Chapter 7. Loop Corporation, a creditor which also owns approximately 50% of the debtors' stock, and various of Loop's affiliates (collectively "Loop") appeal, arguing that the bankruptcy court improperly interpreted and applied 11 U.S.C. § 1112(b). We affirm.

FACTS

Debtor Health Risk Management, Inc. and three of its subsidiaries filed petitions under Chapter 11 of the Bankruptcy Code on August 7, 2001, which the bankruptcy court consolidated and ordered to be jointly administered. The debtors intended from very early in the case to liquidate their businesses rather than attempt to reorganize as viable entities.

In the months following the filing, the debtors successfully liquidated their two primary businesses as well as substantially all of their remaining assets. They used part of the funds from these sales to pay the claims of their secured creditors. As of December 5, 2001, when the debtors filed their initial plan of reorganization, their remaining assets included: 1) approximately $3.25 million in cash; 2) potential causes of action against Ernst & Young and various other directors and accountants of the debtors; and 3) net operating losses that purportedly could provide the estate with $10 million to $20 million in value.[1] The debtors, Loop, and the Official Committee of Unsecured Creditors ("Creditors' Committee") began to attempt to negotiate a consensual plan of reorganization, but they were unsuccessful.

On January 10, 2002, the Trustee moved for conversion of the cases from Chapter 11 to Chapter 7 pursuant to 11 U.S.C. § 1112(b). This motion was opposed by the debtors, Loop, and the Creditors Committee, who sought

---

[1] The purported value of the net operating losses came from the debtors' plan to use the losses to shelter Loop's earnings, with the benefits trickling down to the other unsecured creditors through the issuance of Loop stock.

more time for negotiations. At a February 6, 2002, hearing on the motion, the debtors' counsel explained that the debtors preferred to stay in Chapter 11 and use part of the remaining cash to fund litigation against the accountants and directors rather than distribute the cash to the unsecured creditors. The debtors also believed that the value of the net operating losses could be realized, if at all, only in Chapter 11. Loop and the Creditors' Committee also preferred to remain in Chapter 11 because they thought Chapter 11 had the potential to provide a greater return for the unsecured creditors.

The Trustee, however, focused on the accumulating expenses associated with administering the estate in Chapter 11 – over $1.3 million during the period from September 2001 to January 2002 alone – and the parties' continuing failure to reach a confirmable plan of liquidation. The Trustee believed the expenses would continue to reduce the assets available to the creditors, who would otherwise be entitled to prompt distribution of the remaining cash if the case were conducted under Chapter 7 instead of Chapter 11. *See In re Bell,* 225 F.3d 203, 221-22 (2d Cir.2000) (primary purpose of Chapter 7 trustee is "to collect, liquidate and distribute estate property thereby closing the estate as expeditiously as is compatible with the best interests of the parties") (internal punctuation omitted).

The bankruptcy court concluded at the February 6 hearing that the Trustee had shown cause for conversion. However, the court continued the conversion hearing until March 13, 2002, to give the debtors and creditors one last chance to negotiate a confirmable plan. The parties returned to court on March 13 without having agreed on a satisfactory plan. By that time, even the Creditors' Committee believed conversion to Chapter 7 was appropriate

and had, in fact, filed its own motion for conversion. Only Loop and the debtors opposed.

Relying on its earlier finding of cause and on the Creditors' Committee's new support for conversion, the bankruptcy court granted the motion to convert. Loop appealed the bankruptcy court's conversion order to the district court, which affirmed. Loop now appeals the district court's affirmance.

Although Loop divides its appeal into six separate arguments, we understand it to raise two real issues: first, that the bankruptcy court erred by interpreting § 1112(b) in a manner that Loop believes makes it impossible for liquidating debtors to remain in Chapter 11; and second, that the bankruptcy court abused its discretion by improperly applying § 1112(b) in this case.

I.

The Trustee and Creditors' Committee moved for conversion of the debtors' liquidating Chapter 11 cases to Chapter 7 despite the assertion by Loop and the debtors that a Chapter 11 liquidation would provide greater recovery for the creditors. The bankruptcy court granted the motion to convert because it believed "cause" existed under 11 U.S.C. § 1112(b), which states in part:

> [O]n request of a party in interest or the United States trustee or bankruptcy administrator, and after notice and a hearing, the court may convert a case under this chapter to a case under chapter 7 of this title or may dismiss a case under this chapter, whichever is in the best interest of creditors and the estate, for cause, including –

> (1) continuing loss to or diminution of the estate and absence of a reasonable likelihood of rehabilitation;
>
> (2) inability to effectuate a plan. . . .

The bankruptcy court concluded that cause existed under § 1112(b)(1) because, first, the ongoing expenses associated with administering the estate and attempting to negotiate a confirmable plan constituted "continuing loss to or diminution of the estate" and, second, the debtors were liquidating and therefore had no likelihood of rehabilitation.[2] The court also provided several reasons why it considered Chapter 7 to be better for creditors than Chapter 11, including the court's uncertainty about the

---

[2] The bankruptcy court also apparently believed that cause existed under subsection (2) of § 1112(b), citing its skepticism about whether any plan would be confirmable and the Creditors' Committee's rejection of the debtors' final proposed plan. *See also In re Fossum*, 764 F.2d 520, 521-22 (8th Cir.1985) ("A finding that the [debtors] were unable to effectuate any plan which would be confirmable is a proper basis for dismissal of the [debtors'] chapter 11 case."). However, because the parties disputed whether the bankruptcy court explicitly found cause under § 1112(b)(2), and because a finding of cause under § 1112(b)(1) is a sufficient basis for affirmance, the district court did not examine this potential second ground for conversion. While we agree that the satisfaction of one subsection of § 1112(b) is sufficient to show cause, we see no reason to ignore the bankruptcy court's skepticism about the debtors' ability to confirm a plan. The bankruptcy court is not required, after all, to rigidly apply the enumerated grounds for cause or to analyze one subsection of § 1112(b) in a way that excludes consideration of all other factors favoring conversion. *See, e.g., In re Gonic Realty Trust*, 909 F.2d 624, 626 (1st Cir.1990) (in determining cause "the court may consider other factors as they arise and use its powers to reach appropriate results in individual cases"). Thus, we will consider the bankruptcy court's comments about the debtors' apparent inability to confirm a plan as they are relevant to the court's determination that cause existed and that conversion would serve the best interest of the creditors.

parties' ability to negotiate a confirmable plan and concern about the costs associated with staying in Chapter 11.

We sit as a second court of review in bankruptcy matters and apply the same standards of review as the district court. *See In re Clark,* 223 F.3d 859, 862 (8th Cir.2000). We review the bankruptcy court's factual findings for clear error and its conclusions of law *de novo. See In re Cedar Shore Resort, Inc.,* 235 F.3d 375, 379 (8th Cir.2000). "The bankruptcy court has broad discretion in deciding whether to dismiss or convert a Chapter 11 case." *In re Lumber Exch. Bldg. Ltd. P'ship,* 968 F.2d 647, 648 (8th Cir.1992).

Loop argues that, taken together, the bankruptcy court's interpretations of "continuing loss to or diminution of the estate" and "rehabilitation" mean that cause for conversion to Chapter 7 will automatically exist whenever a debtor seeks to liquidate under Chapter 11. First, Loop asserts, a liquidating debtor will inevitably have a negative cash flow, which the bankruptcy court determined was sufficient to find "continuing loss to or diminution of the estate." Second, a liquidating debtor will by definition have no likelihood of "rehabilitation" because the bankruptcy court understood that term to refer to the restoration of the debtor's business operations, not the liquidation of the debtor's assets. Thus, unless the creditors or Trustee decline to file a motion to convert, a debtor will never be able to liquidate in Chapter 11.

We are unpersuaded by Loop's challenge to the bankruptcy court's interpretation of "continuing loss to or diminution of the estate." Loop concedes that the debtors, as liquidating entities that had ceased their business operations but continued to incur administrative expenses,

had a negative cash flow. Under the interpretation of § 1112(b)(1) consistently used in bankruptcy courts, this negative cash flow situation alone is sufficient to establish "continuing loss to or diminution of the estate." *See, e.g., In re Schriock Constr., Inc.*, 167 B.R. 569, 575 (Bankr.D.N.D.1994) (continuing loss to or diminution of the estate can be established by showing that debtor incurred continuing losses or maintained negative cash flow after entry of the order for relief); *Matter of 3868-70 White Plains Road, Inc.*, 28 B.R. 515, 518 (Bankr.S.D.N.Y.1983) (continuing loss or diminution illustrated by debtor's continual negative cash flow); *see also* 7 *Collier on Bankruptcy* ¶ 1112.04[5][a][i] (Alan N. Resnick & Henry J. Sommer, eds. 15th ed. 2004) ("If the debtor is operating with a sustained negative cash flow after entry of the order for relief, this fact is sufficient to support a finding that the debtor is experiencing a 'continuing loss to . . . the estate.'").

We are convinced that this interpretation is correct, notwithstanding Loop's concern that a liquidating debtor will "inevitably" have a negative cash flow. The purpose of § 1112(b)(1) is to "preserve estate assets by preventing the debtor in possession from gambling on the enterprise at the creditors' expense when there is no hope of rehabilitation." *In re Lizeric Realty Corp.*, 188 B.R. 499, 503 (Bankr.S.D.N.Y.1995). In the context of a debtor who has ceased business operations and liquidated virtually all of its assets, any negative cash flow – including that resulting only from administrative expenses – effectively comes straight from the pockets of the creditors. This is enough to satisfy the first element of § 1112(b)(1), *see In re Citi-Toledo Partners*, 170 B.R. 602, 606 (Bankr.N.D.Ohio 1994) (first requirement of § 1112(b)(1) satisfied because administrative expenses eroded the position of the estate's

creditors and diminished the value of the estate). Thus, the bankruptcy court did not err in finding continuing loss to or diminution of the estate.

Likewise, the bankruptcy court did not err in concluding that a liquidating debtor who had no intention of restoring its business had no reasonable likelihood of rehabilitation. Courts have consistently understood "rehabilitation" to refer to the debtor's ability to restore the viability of its business. *See, e.g., In re Gonic Realty Trust,* 909 F.2d at 627 ("[W]ith no business left to reorganize, Chapter 11 proceedings were not serving the purpose of rehabilitating the debtor's business."); *In re The Ledges Apartments,* 58 B.R. 84, 87 (Bankr.D.Vt.1986) ("Reorganization encompasses rehabilitation and may contemplate liquidation. Rehabilitation, on the other hand, may not include liquidation."); *In re Wright Air Lines, Inc.,* 51 B.R. 96, 100 (Bankr.N.D.Ohio 1985) ("Rehabilitation as used in 11 U.S.C. Section 1112(b)(1) means to put back in good condition; re-establish on a firm, sound basis.") (internal punctuation omitted). Because the debtors here intended to liquidate their assets rather than restore their business operations, they had no reasonable likelihood of rehabilitation.

We are sensitive to Loop's concern that this interpretation of § 1112(b)(1) amounts to a *per se* rule allowing a creditor or Trustee to force conversion to Chapter 7 whenever a debtor seeks to liquidate under Chapter 11. Indeed, it is difficult to imagine a liquidating debtor who will not meet the criteria for cause described in § 1112(b)(1). Nonetheless, this concern may be alleviated if the bankruptcy court's discretion under § 1112(b) is understood to permit the court to deny both conversion and dismissal despite a showing of cause. Such an understanding is

supported by the permissive language of the statute, which states that the court "may" convert or "may" dismiss, and is consistent with our recognition of the bankruptcy court's "broad discretion" under § 1112(b). *See In re Lumber Exch. Bldg. Ltd. P'ship,* 968 F.2d 647, 648 (8th Cir.1992). Allowing the bankruptcy court in an appropriate case to deny dismissal or conversion despite a showing of cause also would give full effect to the statute's admonition to consider the "best interest of creditors and the estate," *see In re Gonic Realty Trust,* 909 F.2d 624, 626-27 (1st Cir.1990) (court has broad discretion under § 1112(b) and may "use its powers to reach appropriate results in individual cases" provided that the ultimate decision is in the best interest of creditors), and would ensure that § 1112(b) is interpreted consistently with the recognition of most courts that liquidation is permitted under Chapter 11. *See, e.g., In re Jartran, Inc.,* 886 F.2d 859, 868 (7th Cir.1989) (liquidating plans permissible under Chapter 11); *Matter of Sandy Ridge Dev. Corp.,* 881 F.2d 1346, 1352 (5th Cir.1989) ("[A]lthough Chapter 11 is titled 'Reorganization,' a plan may result in the liquidation of the debtor.").[3]

---

[3] We recognize some disagreement among lower courts on this subject. *Compare In re Travelstead,* 227 B.R. 638, 651 & n. 14 (D.Md.1998) (liquidating plans are authorized under Chapter 11); *In re Ionosphere Clubs, Inc.,* 184 B.R. 648, 654 (S.D.N.Y.1995) (same), *with In re Lyons Transp. Lines, Inc.,* 123 B.R. 526, 534 (Bankr.W.D.Pa.1991) ("We conclude that there is no authority in the Bankruptcy Code allowing a debtor to file a petition for relief under Chapter 11 for the purpose of self-liquidation."); *Matter of Natrl Plants & Lands Mgmt. Co., Ltd.,* 68 B.R. 394, 395-96 (Bankr.S.D.N.Y.1986) ("Liquidation is not the proper function of reorganization proceedings, but the function of Chapter 7 proceedings."). In any event, we have not located any appellate court cases prohibiting liquidation in Chapter 11 proceedings, and the clear weight of authority permits such liquidation.

In any event, we need not definitively hold that § 1112(b) allows a bankruptcy court to deny conversion or dismissal despite a showing of cause because the bankruptcy court in this case *granted* the motion to convert, which is clearly within the court's discretion once cause has been established. The only question is whether the court abused that discretion.

II.

In considering whether the bankruptcy court abused its discretion, we will assume, as Loop urges, that in addition to finding cause under § 1112(b)(1) the court was under some obligation to consider Loop's evidence purporting to show that the best interest of the creditors and estate would be served by remaining in Chapter 11. *Cf. In re Justus Hospitality Props., Ltd.*, 86 B.R. 261, 265 (Bankr.M.D.Fla.1988) ("The existence of one or more of the grounds set forth [in § 1112(b)] does not compel conversion or dismissal. The bankruptcy court, in its sound discretion, must make the ultimate decision."). Even under such an assumption, the bankruptcy court did not abuse its discretion.

First, there is no merit to Loop's contention that the bankruptcy court erroneously placed the burden of proof on the parties opposing the motion to convert. *See Matter of Woodbrook Assocs.*, 19 F.3d 312, 317 (7th Cir.1994) (moving party bears burden of proving that cause exists under § 1112(b)). Loop bases this argument on comments by the bankruptcy court and Trustee that the debtors had failed to demonstrate how costs would be lower or recovery for creditors higher under Chapter 11 than Chapter 7, which Loop interpreted as indicating a shift of the burden

of proof to the parties opposing the conversion motion. When looked at in the proper context, it is clear that no such shifting occurred and that the bankruptcy court properly held the Trustee to its burden. The court explained why it felt each element of § 1112(b)(1) had been satisfied and specifically concluded, "the U.S. Trustee has shown cause." The court cited the facts it relied upon to support its conclusion, including facts from the debtor's own filings showing administrative expenses and the debtor's undisputed intent to liquidate rather than attempt rehabilitation. The court also gave several reasons why it considered Chapter 7 to be preferable to Chapter 11, including: 1) the court's uncertainty about whether the debtors would ever be able to propose a confirmable plan under Chapter 11; 2) the expenses associated with even attempting to negotiate such a plan; 3) the running of administrative expenses; and 4) the expenses of a disbursing agent and other professionals whose services would be necessary should the parties ever agree on a confirmable plan. Viewed in this light, the comments about the relative costs and benefits of Chapter 7 and Chapter 11 were, at most, a reflection of the court's belief that the parties opposing conversion had failed to produce adequate rebuttal evidence. *See Matter of Woodbrook Assocs.*, 19 F.3d at 317 (debtor has an obligation to produce evidence in opposition to a well-supported motion under § 1112(b)); *In re Lizeric Realty Corp.*, 188 B.R. 499, 503 (Bankr.S.D.N.Y.1995) (once cause is shown, "it is incumbent upon debtor to show that relief under § 1112(b) is not warranted").

Second, we are unpersuaded by Loop's argument that the Trustee did not introduce sufficient evidence to meet its burden of showing cause under § 1112(b). The Trustee

proved the existence of cause by referring to the record, which contained undisputed evidence that the debtors had a negative cash flow and no intention of rehabilitating their business. *See, e.g., In re W. Pac. Airlines, Inc.,* 218 B.R. 590, 595 (Bankr.D.Colo.1998) ("[I]t cannot be denied that the Committee has established 'cause' under Section 1112(b) by showing that not only does the Debtor lack the ability to reorganize, but that it also has had a negative cash flow since the filing of this case."). The record also showed the debtors' failure to achieve a confirmable plan with the creditors, thus indicating that the negative cash flow and non-payment of unsecured creditors would continue indefinitely if the case remained in Chapter 11. Conversion to Chapter 7, on the other hand, would eliminate the expenses associated with confirmation of a plan and likely would ensure prompt distribution of the remaining cash to the unsecured creditors. *See In re Bell,* 225 F.3d 203, 221-22 (2d Cir.2000) (primary purpose of Chapter 7 trustee is "to collect, liquidate and distribute estate property thereby closing the estate as expeditiously as is compatible with the best interests of the parties") (internal punctuation omitted). Finally, the record showed that the debtors' desired Chapter 11 plan would result in the expenditure of even more cash in the pursuit of various causes of action. Because such causes of action could be pursued by a trustee in Chapter 7, *see, e.g., In re Ozark Rest. Equip. Co., Inc.,* 816 F.2d 1222, 1225 (8th Cir.1987) (Chapter 7 trustee has the responsibility to assert any causes of action necessary for collection or preservation of the estate because "estate property" includes causes of action), no advantage would be gained by remaining in Chapter 11; instead, time and resources would be wasted during a confirmation process that may never even be successful.

Loop nonetheless claims that the debtors presented "unrefuted" evidence in opposition to the conversion motion, including, in particular, a self-serving affidavit purporting to demonstrate the value of the net operating losses in Chapter 11. Although there was no evidence directly refuting the net operating loss issue, the bankruptcy court was not required to blindly accept the debtors' allegations as fact. Instead, the court should, and did, assess the evidence critically and assign it only the weight it deserved. We see no abuse of discretion in the court's ultimate conclusion that any speculative value which might be derived from the net operating losses in Chapter 11 was outweighed by the continuing erosion of the estate, the debtors' failure to achieve a confirmable Chapter 11 plan, and the preference of the Creditors' Committee for conversion. *See In re Tiana Queen Motel, Inc.,* 749 F.2d 146, 151-52 (2d Cir.1984) (affirming conversion order where debtor's prospects for reorganization were based on nothing more than the "boundless confidence" of one of the debtor's principals); *Quarles v. U.S. Trustee,* 194 B.R. 94 97 (W.D.Va.1996) (affirming conversion order where debtor's hope to improve his financial problems through litigation was "pure speculation").

Third, we conclude the bankruptcy court made sufficient findings of fact to support its conversion order. The court gave an extensive oral explanation for its grant of the conversion motion, stating, *inter alia*: "as we sit here the administrative expenses are running. That diminishes the estate. . . . No rehabilitation is proposed here . . . rehabilitation does not encompass what the debtor is doing here so cause has been shown. . . . Maybe I'm missing something but I'm not missing the expense that is going to be involved in consummating this plan. . . . The estates are

continuing to incur losses and it's being diminished and there is no opportunity or [chance] for rehabilitation." The court also listed the reasons it considered Chapter 7 to be preferable to Chapter 11. These findings are adequate. *See In re Fossum,* 764 F.2d 520, 521-22 (8th Cir.1985) (bankruptcy court's factual findings sufficient despite consisting of a single sentence: "the debtors must realize that reorganization is simply not possible and [that] liquidation is the only feasible alternative"); *Matter of Koerner,* 800 F.2d 1358, 1368 (5th Cir.1986) ("The bankruptcy judge is not required to give exhaustive reasons for his decision [to convert].").

Finally, the conversion order was not premature and did not impermissibly deprive the creditors not represented on the Creditors' Committee of the opportunity to consider the debtors' final proposed plan of reorganization. *See Woodbrook Assocs.,* 19 F.3d at 317 ("Creditors need not wait until a debtor proposes a plan or until the debtor's exclusive right to file a plan has expired. . . . The very purpose of § 1112(b) is to cut short this plan and confirmation process where it is pointless."). In fact, the role of the creditors' committee would be obliterated if, as Loop seems to suggest, the bankruptcy court is required to solicit the views of the entire body of creditors each time a debtor proposes a new plan. *See Matter of Advisory Comm. of Major Funding Corp.,* 109 F.3d 219, 224 (5th Cir.1997) ("Creditor Committees have the responsibility to protect the interest of the creditors; in essence, the function of a creditors' committee is to act as a watchdog on behalf of the larger body of creditors which it represents.") (internal punctuation omitted). We are satisfied that the Creditors' Committee's consideration and rejection of the debtors' plan, combined with the bankruptcy court's findings under

§ 1112(b)(1), is sufficient to justify the timing of the bankruptcy court's order.

III.

We conclude that the district court properly interpreted § 1112(b) and did not abuse its discretion in ordering conversion of the debtors' case to Chapter 7. We affirm.

290 B.R. 108

LOOP CORP., Leon Greenblatt, Nola, LLC, Repurchase Corp., Leslie Jabine, Teletech Systems, Inc., Chiplease, Inc., and Banco Panamericano, Appellants,

v.

UNITED STATES TRUSTEE, and Committee of Unsecured Creditors, Appellees.

No. Civ.02-793 ADM.

United States District Court,
D. Minnesota.

Feb. 5, 2003.

Michael F. McGrath, Ravich Meyer Kirkman McGrath & Nauman, P.C., Minneapolis, MN, and Robert M. Fishman, and Brian L. Shaw, Shaw Gussis Fishman Glantz & Wolfson, LLC, Chicago, IL, on behalf of Appellants.

Michael R. Fadlovich, U.S. Trustee's Office, Minneapolis, MN, on behalf of Appellant U.S. Trustee.

MEMORANDUM OPINION AND ORDER

MONTGOMERY, District Judge.

I. INTRODUCTION

This matter is before the undersigned United States District Judge on Appeal [Docket No. 1] from the March 13, 2002 Order of Bankruptcy Judge Robert J. Kressel [Docket No.1, Doc. No. 2]. Appellants challenge the court's conversion of the consolidated bankruptcy cases

[Bky 01-43354] of Debtors Health Risk Management, Inc., HRM Claim Management, Inc., Institute for Healthcare Quality, Inc., and Health Benefit Reinsurance, Inc. f/k/a Health Benefit Reinsurance of Michigan, Inc. (collectively, "Debtors"), from Chapter 11 to Chapter 7. This matter was taken under advisement on November 15, 2002, upon the filing of Appellants' Reply Brief. For the reasons stated below, the Appeal is denied and the March 13, 2002 Order is affirmed.

II. BACKGROUND

Debtor Health Risk Management ("HRM") is a parent corporation with several subsidiaries. On May 18, 2001, Ernst & Young resigned as HRM's independent auditors after issuing a restatement of HRM's payables to reflect a $6 million increase. After revelation of Ernst & Young's mistake, Loop Corporation ("Loop"), owner of roughly 50% of HRM's stock, notified HRM that it would not fund the remaining $3.1 million of financing under an agreement in which Loop had committed to provide $6.1 million to HRM. Debtors' Disclosure Statement of Dec. 5, 2001, at 7 ("Disclosure Statement") [Docket No. 1, Doc. No. 9]. As a result of liquidity problems, on August 7, 2001, HRM and three of its subsidiaries filed four Chapter 11 cases [Bky 01-43354; Bky 01-43355; Bky 01-43356; Bky 01-43357], now consolidated and jointly administered under Bky 01-43354.

By December 5, 2001, HRM had liquidated most of its assets and filed its Disclosure Statement and Plan of Liquidation. Disclosure Statement at 1. HRM had no ongoing business concerns. Its assets consisted of: 1) approximately $3.25 million in cash; 2) potential causes of

actions against Ernst & Young, Loop, and directors and accountants of HRM; and 3) net operating losses ("NOLs"). The Official Committee of Unsecured Creditors ("Committee"), HRM, and Loop then entered into roughly two months of negotiations on how to proceed. From September, 2001, through January, 2002, expenses and fees of attorneys, accountants, and consultants totaled over $1.3 million, and no final agreement was reached. *See* Bky 01-43354 Docket Nos. 71, 100, 103, 111, 160, 180, 206, 207, 209, 213, 224, 225, 236, 266, and 267 (applications for fees and expenses).

By motion heard on February 6, 2002, the U.S. Trustee ("UST") asked for the Chapter 11 case to be dismissed or converted to Chapter 7 [Docket No. 1, Doc. Nos. 11, 12; Bky 01-43354 Docket No. 238]. The UST argued that the government trustee appointed to oversee the Chapter 7 action would have lower management expenses and expedite the process of securing payment for the creditors. Tr. of 2/6/02, at 6-11. Referencing the fruitless negotiations of the prior two months and the attendant expenses, it asserted that continued Chapter 11 proceedings would bring a certainty of more legal and consulting costs in exchange for the mere possibility of bringing in revenue for the NOLs. *Id.* at 7. In the UST's opinion, the plan developed by HRM seemed cumbersome and unlikely to work. *Id.* at 7, 9-11. The UST argued that the creditors would be better off avoiding certain expenses for the slim chance of greater return, and, based on his review of the December 5, 2001 Debtors' Plan of Liquidation ("Plan"), Judge Kressel agreed. However, all the parties involved, Debtors, Appellants, and the Committee, wanted to pursue the Plan and claimed that they were merely days away from an agreement. Judge Kressel expressed his inclination to convert, but continued the case

until March 13, 2002, to give the parties a chance to finalize a reorganization plan. He warned the parties that if all had not agreed to a final plan by March 13, he would convert the case. *See* Tr. of 2/6/02, at 38, ll. 14-25.

On Monday, March 4, 2002, the Committee changed its position, filing a motion requesting that the case be converted to Chapter 7 immediately, or alternatively that HRM's assets be frozen pending the March 13 hearing. *See* Motion for Expedited Hearing and Immediate Convers on ¶¶ 17, 18 [Docket No. 1, Doc. No. 22]. As a basis for its motion and exigency, the Committee alleged sudden management changes, stating that on or about February 28, 2002, all of the members of HRM's board of directors resigned, with the exception of Andrew Jahelka ("Jahelka"). *Id.* ¶ 12. Jahelka thus simultaneously held positions as the sole member of HRM's board and as president of Loop, in addition to being a target of litigation in the Chapter 11 proceedings. *Id.* ¶ 14; *but see* Debtors' Response to Committees' Motion ¶ 3 [Docket No. 1, Doc. No. 24] (stating that the management shift was a minor change because there were only two directors prior to the resignation). Further, the Committee stated that Jahelka, as the sole director of HRM's board, then appointed Leon Greenblatt ("Greenblatt"), the majority owner of Loop and holder of ownership interests in other Appellants, as chief restructuring officer of HRM. Motion for Expedited Hearing and Immediate Conversion ¶¶ 14, 16. Stating that such changes placed Debtor HRM entirely under the control of just the Appellant creditors, the Committee argued that the requested relief was necessary to prevent insider control and usurpation of Debtors' assets. *Id.* ¶¶ 14, 16, 17. Judge Kressel heard the Committee's arguments in favor of conversion on March 7, but continued the motion

without decision until the previously scheduled hearing on March 13. Tr. of 3/7/02, at 13, l. 2.

At the March 13 hearing, Loop and HRM presented a plan on which the two had agreed. The Committee and the UST opposed this plan and requested that the case be converted to Chapter 7. Referencing his earlier findings and statement that unless all the parties had agreed to a final plan he would convert the case, Judge Kressel converted the case to Chapter 7. Appellant: now contest this ruling.

Appellants raise six issues on appeal. All center around the interpretation of 11 U.S.C. § 1112(b) and the sufficiency of the evidence. Initially, Appellants claim Judge Kressel applied improper legal standards under § 1112(b)(1). Second, they argue he failed to hold Appellees, as movants, to their burden of proof. Relatedly, it is asserted that Appellees did not introduce sufficient evidence to support the conversion. Next, Appellants contend the bankruptcy court erred in failing to make adequate findings of fact. Fifth, they allege the bankruptcy court did not give proper weight to certain evidence, and lastly, that they were deprived of the opportunity to present their revised plan, resulting in a premature ruling.

III. DISCUSSION

A. Standard of Review

The District Court reviews the Bankruptcy Court's factual findings for clear error and conclusions of law de novo. *In re Svoboda,* 264 B.R. 190, 194 (8th Cir. BAP 2001). A finding is clearly erroneous if the reviewing court "is left with a definite and firm conviction that a mistake

has been committed." *Id.* The bankruptcy court has broad discretion in evaluating whether or not there is cause to convert a Chapter 11 case and the court's factual basis for this determination will be reversed only for clear error. *In re Hatcher,* 218 B.R. 441, 448, 449 (8th Cir. BAP 1998); *In re Lumber Exch. Build. Lmt. P'ship,* 968 F.2d 647, 648 (8th Cir.1992).

B. 11 U.S.C. § 1112(b)

11 U.S.C. § 1112(b) provides that the court may convert a Chapter 11 case to a case under Chapter 7 if such action is in the best interests of the creditors and the estate, and cause for conversion exists. 11 U.S.C. § 1112(b); *see also In re Fort Knox Mini Warehouse, Inc.,* 2002 WL 1842452, at *2 (Bankr.N.D.Iowa July 31, 2002). This section enumerates nine alternative factors that constitute cause. 11 U.S.C. § 1112(b). The list is not exhaustive and courts may find cause for other equitable reasons. *See In re Economy Cab & Tool Co.,* 44 B.R. 721, 724 n. 1 (Bankr.D. Minn.1984). Among other circumstances, the statute states that cause includes "(1) continuing loss to or diminution of the estate and absence of a reasonable likelihood of rehabilitation; (2) inability to effectuate a plan; [or] (3) unreasonable delay by the debtor that is prejudicial to creditors. . . ." 11 U.S.C. § 1112(b). The movant bears the burden of proof and must demonstrate the presence of one of he [sic] statutory grounds or other cause. *Economy Cab,* 44 B.R. at 724.

Though some dispute exists as to the number of factors under which the court found cause to convert, the record shows Judge Kressel decided that cause had been established under the first statutory circumstance, continuing

loss to or diminution of the estate coupled with no reasonable likelihood of rehabilitation. *See* 11 U.S.C. § 1112(b)(1); Tr. of 2/6/02, at 36-37, II. 18-15. Because one ground for cause is sufficient standing alone, the Court need not discuss the parties arguments as to additional factors listed in § 1112(b).

The first ground requires a showing of both a continuing loss to the estate and the absence of a reasonable likelihood of rehabilitation. 11 U.S.C. § 1112(b)(1). A finding that the debtor suffered continuing losses or maintained a negative cash flow "after the entry of the order for relief" suffices to demonstrate continuing loss to the estate. *Fort Knox,* 2002 WL 1842452, at *2. Absence of likelihood of rehabilitation is satisfied by a showing that the debtor is unable to get the business up and running again on a firm base. *In re Minnesota Alpha Found.,* 122 B.R. 89, 93 (Bankr.D.Minn.1990); *Economy Cab,* 44 B.R. at 725 n. 2. Under § 1112(b), "'rehabilitation' contemplates the successful maintenance or re-establishment of the debtor's business operations. . . ." *Minnesota Alpha,* 122 B.R. at 93.

a. Continuing Loss

Citing case law from other jurisdictions, Appellants complain that the court incorrectly considered the continuing administrative expenses to constitute diminution of the estate. In doing so, they assert, the court created a per se rule that there will be cause for conversion in every liquidating Chapter 11 case. However, within the Eighth Circuit, continuing loss can be demonstrated by a bare showing that the debtor suffered continuing losses or maintained a negative cash flow position after the entry of

the order for relief. *Fort Knox,* 2002 WL 1842452, at *2; *In re Schriock Const.,* 167 B.R. 569, 575 (Bankr.N.D.1994). The debtors do not dispute that losses were continuing, but base their argument on the court's interpretation of the law. The transcript of the proceeding reveals that Judge Kressel properly applied the standard used in this Circuit and Appellants' attempt to insert their preferred version of the law must be rejected. *See* Tr. of 2/6/02, at 12-13, ll. 20-13, 36-37, ll. 18-15; *In re Schriock,* 167 B.R. at 575. Although not a required finding under the law of the Eighth Circuit, Judge Kressel further noted that costs would likely be less under Chapter 7 than Chapter 11, due to the complexity of the Plan and the mounting legal and administrative costs. *See* Tr. of 2/6/02, at 33-34, ll. 20-7, 34-35, ll. 22-14, 36, ll. 14-17. In considering these litigious and discordant circumstances of the dispute the court properly made "a full evaluation of the present condition of the estate." *Economy Cab,* 44 B.R. at 724.

b. Likelihood of Rehabilitation

Similarly, Judge Kressel's conclusion that rehabilitation was not reasonably likely was not clearly erroneous. *See Minnesota Alpha,* 122 B.R. at 93; *Economy Cab,* 44 B.R. at 725 n. 2. The Debtor's Disclosure Statement reveals that HRM had no ongoing business concerns and Appellants do not contest that they had no intent to re-establish the business. *See* Disclosure Statement at 1. Instead, they again rely on the statutory interpretations of other jurisdictions, claiming that rehabilitation requires only the ability to confirm a plan of reorganization, not the ability to "emerge as an economically viable enterprise." *In re Schriock,* at 576.

The bankruptcy court's findings on this point, based on the record before it, properly applied the precedent of this Circuit and evidenced consideration of multiple factors. *See Minnesota Alpha,* 122 B.R. at 93 (reciting that "[r]ehabilitation means something more than reorganization," and noting that the prospect of long and complicated litigation militated against likelihood of rehabilitation) (internal quotation and alterations omitted); Tr. 2/6/02, at 12-13, ll. 20-13, 29, ll. 14-24, 36-37, ll. 25-6.

Even if the court's application of these legal standards to the facts of this case implied a per se rule of cause, the court has broad discretion in determining cause and is not limited to grounds specified in § 1112(b), such that the conversion may be supported on multiple bases. *See Economy Cab,* 44 B.R. at 724 n. 1. A bankruptcy judge may find cause for equitable reasons beyond those exemplified in § 1112(b), and Judge Kressel not only found continuing losses and lack of rehabilitation, but that the state of affairs between the parties warranted conversion. *Id.;* Tr. of 2/6/02, at 33-34, ll. 20-7, 34-36, ll. 18-17. The court's consideration of factors such as the potential for conflicts, the complicated and costly nature of the Plan, and his view, based on review of the Plan, that it would not be confirmable, informed his decision to convert. Tr. of 2/6/02, at 33-34, ll. 20-7, 34-36, ll. 18-17. This was not an abuse of discretion.

c. The Best Interests of the Creditors

In addition to finding cause under any factor, the court must determine whether conversion or dismissal is in the best interests of the creditors. 11 U.S.C. § 1112(b); *Han v. Linstrom,* 2002 WL 31049846, at *4 (N.D.Ill. Sept.12, 2002).

The court does not need to consider whether or not proceeding under Chapter 11 would be better, but only whether conversion or dismissal is preferable. *See id.* (citing *In re Woodbrook Assocs.,* 19 F.3d 312, 316 (7th Cir.1994)). Appellants contend that the bankruptcy court failed to make any findings regarding this necessary determination. However, the proceedings reveal that after Judge Kressel found cause, he also considered whether conversion or dismissal would be best, as required. *See* Tr. of 2/6/02, at 37, ll. 8-15; Tr. of 3/13/02, at 33, ll. 5-20.

C. Movant's Burden of Proof

As another ground of attack, Appellants argue Judge Kressel improperly shifted the burden of proof from the movant, the UST, to the Appellants. The February 6, 2002 Transcript, however, specifically states the court's recognition of the movant's burden and its conclusion that the movant had established cause. *See* Tr. of 2/6/02, at 37, ll. 8-15. Once cause has been shown, the judge may shift the burden of proof to the debtor to demonstrate that Chapter 11 would be better than Chapter 7. *Minnesota Alpha,* 122 B.R. at 94. This is precisely what occurred in this case. Judge Kressel gave Appellants the opportunity to present him with an agreed-upon, confirmable plan and the debtor failed to meet this burden. Tr. 2/6/02, at 37-39, ll. 16-4. Accordingly, at the subsequent hearing, Judge Kressel found cause pursuant to his earlier determinations. Tr. of 3/13/02, at 32-33, ll. 19-20. The allocation of the burden was proper under the law. *Minnesota Alpha,* 122 B.R. at 94.

D. The Court's Findings of Fact

Appellants next assert that the court did not make sufficient findings of fact. Particularly, Appellants challenge Judge Kressel's basis for his conclusion that conversion was in the best interests of the creditors.

An order of conversion does not require extensive findings of fact. Findings merely need to be sufficient to allow a reviewing court to determine the basis of decision. *In re Fossum,* 764 F.2d 520, 521-22 (8th Cir.1985); *see also In re Sunflower Racing, Inc.,* 226 B.R. 665, 671 (D.Kan.1998). Judge Kressel specifically found, based on the Debtors' statements and disclosures, his personal review of the Plan and conclusion that it was excessively complex and costly, and the Committee's refusal of the proposed plan, as the representative body for the unsecured creditors, that conversion was proper. *See* Tr. of 2/6/02, at 33-39; Tr. of 3/13/02, at 33, ll. 13-20.

After reading the Plan, Judge Kressel determined that it was overly complicated and unlikely to be confirmed. Tr. of 2/6/02, at 34, ll. 8-10, 35, ll. 6-8, 35-36, ll. 25-11. Considering the contents of the Plan, the fact that several of the parties had already threatened, and the Committee had actually filed a motion to commence litigation against one another, along with the $1.3 million in legal, accounting and consulting expenses that had already accumulated, Judge Kressel found cause. He inferred that given the complicated nature of the Plan, and the disputes between the parties, it might not be possible to effectuate a Chapter 11 plan at all and, even if it were possible, it would require much more negotiation and possibly even litigation. *Id.* at 33-38. From the amount of the fees already incurred, Judge Kressel considered that

continuing on this course would be very expensive. Further, Judge Kressel concluded that conversion was in the best interests of the creditors, noting that the Committee favored conversion and that these creditors were in the best position to determine their own best interests. *See* Tr. of 3/13/02, at 33, ll. 14-18. These factual determinations are sufficient to support conversion under the law and were not clearly erroneous. *See e.g., Allied Van Lines, Inc. v. Small Bus. Admin.,* 667 F.2d 751, 753 (8th Cir.1982) ("It is well established that the trial court does not need to make specific findings on all facts but only must formulate findings on the ultimate facts necessary to reach a decision.").

E. Movant's Evidence

Appellants cite no authority for the proposition that the UST may not rely on evidence of the debtor's circumstances already in the record to meet its burden of proof. In fact, in *Fort Knox,* the bankruptcy court stated that the trustee was relying on the debtor's financial statements and proceeded to find continuing losses based on this evidence. *Fort Knox,* 2002 WL 1842452, at *1-2, 3, 7 (discussing debtor's profit and loss statements; concluding with dismissal). Here, the UST acknowledged its evidentiary basis for its argument and the court explicitly articulated that the UST had shown cause with this proof. Tr. of 2/6/02, at 29, ll. 15-24, 37, ll. 8-12. Despite these allegations of insufficient evidence, Appellants do not dispute the court's factual findings regarding losses and rehabilitation, but instead challenge Judge Kressel's recitation and application of the legal standards of § 1112(b)(1), which, as addressed above, were proper. That much of the support for Appellees' motion and the court's decision came

from Appellants' and Debtors' own submissions, which they do not dispute, does not detract from the sufficiency of the movant's factual basis.

F. Failure to Give Proper Weight to the Value of the NOLs

Without supporting citation, Appellants aver that the court abused its discretion by giving insufficient weight to the value of the NOLs. This exercise of judgment was not an abuse of judicial discretion. Indeed, under the standards of this Circuit, it is not clear that Judge Kressel even needed to consider this evidence. *See e.g., Fort Knox,* 2002 WL 1842452, at *2-3 (reciting tests for cause under § 1112(b)(1)). The NOLs would not have altered HRM's present negative cash flow, nor would they have gotten the company up and running again. Thus, cause would still exist. Similarly, the best interest of the creditors test requires consideration of conversion versus dismissal, not conversion versus benefits that might be realized under Chapter 11 or other alternatives. *See Woodbrook,* 19 F.3d at 316.

G. Premature Conversion/Failure to Hear Evidence

As another basis of appeal, it is asserted that the court erroneously denied Appellants the opportunity at the March 13, 2002 hearing to present evidence regarding the new proposed plan. Motions for conversion do not require full evidentiary hearings but only an adequate record on which to determine the relevant issues. *Sunflower Racing,* 226 B.R. at 671. Judge Kressel expressly informed Appellants what they needed to do to withstand conversion, i.e., present an agreed-upon plan. Tr. of 2/6/02, at 33. Having

been unable to fulfill this condition, Appellants were not entitled to enter in evidence the attributes of their revised plan. *See Sunflower Racing,* 226 B.R. at 671; *Minnesota Alpha,* 122 B.R. at 94 (stating that burden of proof shifts to opponent once movant has shown cause).

IV. CONCLUSION

Based on the foregoing, and all the files, records and proceedings herein, **IT IS HEREBY ORDERED** that:

1. Appellants' Appeal [Docket No. 1] is **DENIED**, and

2. The March 13, 2002 Order of Bankruptcy Judge Robert J. Kressel [Docket No. 1, Doc. 2; Bky 01-43354 Docket No. 296] is **AFFIRMED**.

LET JUDGMENT BE ENTERED ACCORDINGLY.

UNITED STATES BANKRUPTCY COURT
DISTRICT OF MINNESOTA

[MAR. 14, 2002]

In re:

Health Risk Management, Inc.,	BKY 01-43354
HRM Claim Management, Inc.,	BKY 01-43355
Institute for Healthcare Quality, Inc.,	BKY 01-43356
Health Benefit Reinsurance, Inc., f/k/a Health Benefit Reinsurance of Michigan, Inc.,	BKY 01-43357
Debtors.	ORDER OF CONVERSION

At Minneapolis, Minnesota, March 13, 2002.

These cases came on for hearing on motions by the United States Trustee and by the Committee of Unsecured Creditors to convert the cases to cases under chapter 7. Michael J. Fadlovich appeared for the United States Trustee, Nancy Peterman and James A. Rubenstein appeared for the Committee, James L. Baillie appeared for the debtors, and Robert M. Fishman appeared for Loop Corporation.

Based on findings of fact and conclusions of law stated orally and recorded in open court,

IT IS ORDERED: These cases are converted to cases under chapter 7.

/s/ Robert J. Kressel
ROBERT J. KRESSEL
UNITED STATES
BANKRUPTCY JUDGE

UNITED STATES BANKRUPTCY COURT
DISTRICT OF MINNESOTA
MINNEAPOLIS, MINNESOTA

In re: HEALTH RISK MANAGEMENT, Debtor	Docket No. BKY 01-43354
HRM CLAIM MANAGEMENT, INC., Debtor.	Docket No. BKY 01-43355
INSTITUTE FOR HEALTHCARE QUALITY, INC., Debtor.	Docket No. BKY 01-43356
HEALTH BENEFIT REINSURANCE, INC., Debtor.	Docket No. BKY 01-43357 Minneapolis, Minnesota February 6, 2002

TRANSCRIPT OF HEARING
ON MOTION SO BEFORE THE
HONORABLE ROBERT J. KRESSEL
UNITED STATES BANKRUPTCY JUDGE

Appearances:

For Debtor: JAMES BAILLIE, ESQ.
Frederickson & Byron
900 2nd Avenue South
Suite 1100
Minneapolis, MN 55402

and

	MICHAEL McKIM, ESQ. 292 Fairmont Avenue St. Paul, Minnesota 55105
[2] For Unsecured Creditors Committee:	JAMES RUBENSTEIN, ESQ. Moss & Barnett 4800 Wells Fargo Center 90 South 7th Street Minneapolis, Minnesota 55402
	NANCY PETERMAN, ESQ. Greenberg & Traurig 77 West Wacker Drive Suite 2500 Chicago, Illinois 60607
For the U.S. Trustee:	MICHAEL FADLOVICH, ESQ. Office of the U.S. Trustee 1015 U.S. Courthouse 300 South 4th Street Minneapolis, Minnesota 55415
For Creditor, Loop Corporation and Loop Entities:	ROBERT FISHMAN, ESQ. 1144 West Fulton Street Suite 200 Chicago, Illinois 60607
	and
	MICHAEL McGRATH, ESQ. Ravich, Meyer, et al 80 South 8th Street Suite 4545 Minneapolis, Minnesota 55402
Court Recorder:	Kathy Barksdale U.S. Bankruptcy Court Minneapolis, Minnesota

* * *

[12] for several days as to how to begin because I find the motion very mysterious and hard to – hard to get ahold of and I found this statement in the U.S. Trustee's reply that helped explained to me why I was having trouble with this. The quote is the unsecured creditors can make no factual showing whatsoever that their position will somehow be harmed by the conversion of the case. In the absence of such a showing the cases must be converted and the problem is that what we have in front of the Court is an expression of preference in the United States Trustee's office to Chapter 7 over liquidating plans in Chapter 11.

Now we happen to disagree with that, happen to disagree with it vehemently, but it has nothing to do with the motion now before the Court because the U.S. Trustee's motion provides no – no factual support in favor of its motion even though it has the burden of proof. It ties its arguments to no statutory standard in Section 1112 and makes a number of other arguments which are contrary to the facts that are in front of the Court and so we find this situation difficult to deal with.

THE COURT: Let's start with this. Is there any – it seems to me one of the grounds for conversion or dismissal is a diminution of the estate and the lack of some likelihood of rehabilitation and those both exist here, don't they? The estate is diminishing. Certainly there is no assets coming in and there is expenses accruing and the debtor is not going to be [13] – debtors are not being rehabilitated so grounds have been shown for conversion or dismissal right there, aren't they?

MR. BAILLIE: Well, rehabilitation in this context, Your Honor, I think has to include a plan of

reorganization. The standards of Section 1123 which permit a plan under which the sale and distribution will occur under a plan of reorganization.

THE COURT: Well, I think the case law is quite to the contrary, that reorganization can include liquidation like this but rehabilitation means something quite different. It means getting businesses up and going and running again. That's what rehabilitation is. You don't rehabilitate debtors by sucking all the assets out and giving them away.

MR. BAILLIE: Well, Your Honor, if – first of all they have cited no authority for that or no – no facts so the record is really bare on that fact but if that – if that is taken to be to require conversion then there can never be a liquidating plan because rehabilitation according to the reading that the Court just offered is not included, and yet the Bankruptcy Code is clear that that method of completion of a Chapter 11 case is appropriate within the Chapter 11 context.

And in addition diminution of the estate wouldn't be accurate in this situation and even liquidation – to suggest that the liquidation is over is not accurate since there is considerable litigation to be brought and the expectation that

* * *

[29] statement in the U.S. Trustee's pleading there was no citation of law, statutory or case, to support that statement and that's because of course there is no law that says that, and with all due respect to the United States Trustee's obligation to administer these cases and there are very real interests in obtaining the best outcome for creditors

that they can when you have a case with active and competent participants who are trying to protect their own economic interests I think that deferral to the U.S. Trustee's view of how the process should work is not appropriate, and I heartily request that the Court deny the motion of the U.S. Trustee and allow the parties a chance to see if they can realize the value that they believe may exist. Thank you, Your Honor.

THE COURT: Mr. Fadlovich, anything you wanted to add?

MR. FADLOVICH: Yes, Your Honor. I guess I thought it was pretty obvious what the U.S. Trustee was lying – relying on as the factual basis for her motion and that is the record in this case. The record of the Court orders approving the sales of the assets, the record of the debtor's plan and disclosure statement which makes the representation that the sales have been consummated and there is no business left, the unsworn declaration of Mr. LeBlanc regarding the existence of $121 million in claims, the schedule, the claims register, everything that is in the record.

What we don't have in the record is anything from the [30] debtor explaining how the numbers work so that going forward in Chapter 11 gives creditors more money. You know, as we stand here I have no clue what a Dutch auction is. The debtors haven't proffered anything that would establish that. It is the U.S. Trustee's position that the burden of proof has been met by virtue of the facts in the record, the admissions of the debtor and the other parties in interest in their pleadings, and on that basis cause exists to convert the case.

The net operating loss issue is, you know, a relatively small issue in the scheme of things. I think the Court can rely on nothing more than the ongoing losses to or diminution of the estate and absence of reasonable likelihood of rehabilitation. There is no likelihood that any payment to creditors will be enhanced under the scenario we have here because if there was the debtors and all the parties who have been involved in this would have brought forward a witness and said this is now the numbers are going to work and this is why more money is going to come in if we are allowed to go forward, but they haven't done that.

All they have done is gone through the steps of liquidating these assets and they did do a good job liquidating the assets but it's over and when it's over it's over and they ought to recognize the fact and on that basis I think the Court needs to convert these cases today.

THE COURT: Anything else over on this side of the

* * *

[32] the presentation that the United States Trustee suggests we ought to be in a position to make. Thank you, Your Honor.

MS. PETERMAN: Your Honor, I just wanted to raise two other points. The United States Trustee mentions that there is no evidence in the record I guess from this side of the room as far as why a Chapter 11 liquidating plan is more beneficial to the creditors, why the creditors might get a better outcome under that scenario, and there is a liquidation analysis attached to the debtor's plan which does show that the creditors are better off

through the Chapter 11 liquidating plan versus Chapter 7 case, and I mean just –

If you just look at the Bankruptcy Code once you have the Chapter 7 trustee come into place that will cost the creditors money because the Chapter 7 trustee will be entitled to a fee on top of whatever other administrative expenses exist. In addition there has been a lot of talk about the ongoing or continuing losses that are occurring with respect to the estate and we don't – we do not have an operating business at this time and I would characterize what is happening as far as losses more as kind of a plateau.

There are certainly expenses of administration but there is going to be expenses of administration whether they are in Chapter 11 or Chapter 7. I'm not sure that there is going to be any less of an expenditure of estate funds in Chapter 7.

MR. BAILLIE: Your Honor, to go back to the question [33] that the Court asked in the beginning we have indicated – whether it's a continuing loss requires I think a longer look here than the short period of time that we have involved or diminution of the estate. We think that the estate will be augmented by the process that we are on and the absence of a reasonable chance of rehabilitation should include the chance of the liquidation plan under Section 1123 and finally that is only an example under which the Court has some discretion and we think in this situation the discretion ought to be exercised not to convert the case.

That is a may in Section 1112 and many good reasons have been offered here why all the parties are better off if we have a longer look at this case. Thank you.

THE COURT: Well, I confess I went back and forth on this as I was spending a lot of time going through the file and as I started I suspected I was prepared to deny the motion because the debtors were far down the road towards getting a plan confirmed and it made some sense for that to go forward, but then as I got farther in yet again I started looking at what looks to me, and it is hard to quantify, no one has really quantified this, as an enormous expense that is going to – enormous is a relative word – a lot of expense that is going to sustained both to confirm a plan and to consummate this plan.

I'm looking at – you know, I'm told here now the committee and the debtors are close. I don't know what that [34] means but a lot of money has been spent all coming out of the creditors' pockets obviously to pay the debtor's lawyers and the committee's lawyers, of which there are two, to even agree on a plan, and I don't know where that's going but in the meantime while that is all going on the estate is incurring the expense of paying the debtor and its – debtors and their professionals and the committee and its professionals.

I look at the plan. I'm even concerned that – even if that's all done I'm very concerned about the confirmability of it even if we got there. While I was dismissed out of hand by the debtor at the last confirmation hearing I am deeply concerned about the classification issue. I don't know how you can take the creditors of four different legal entities and put them in one class. Proper classification requires creditors to have substantially similar interests to be in the same class and I don't know how a creditor who is a creditor of one debtor can be substantially similar to a creditor of another debtor.

So I'm very concerned if you go through this all this process the plan wouldn't even be confirmable leaving out the other issues that have been raised indirectly by people who are objecting to the disclosure statement so that the confirmation process itself would not be cheap. It would incur expense both for the debtors' professionals and the committee's professionals with no guarantee that that plan is ever going to get confirmed.

The committee has brought a motion it wants authority [35] to bring some lawsuits which is inconsistent with provisions in the debtors' plan. I don't know how that fights but it is a fight and fights cost money. Disputes cost money. As part of that the committee has brought its Rule 2004 motion and its motion to be given authority to bring these actions.

Frankly as I looked at the plan it seemed me to for a case of this size at least unduly complicated and thus expensive. After confirmation if we even go that far we are looking at a disbursing agent who would have to be paid. He is entitled to hire lawyers who would want to be paid and maybe other professionals who would want to be paid, all of this money coming out of creditors' pockets. There is a steering committee who apparently aren't compensated but all of their expenses are going to be paid.

I'm looking forward to battles between the steering committee and the disbursing agent over various actions so it kind of undermines the independent judgment of such a disbursing agent which is I guess the idea but it certainly can lead to conflicts and conflicts cost money. I am bothered – leaving aside and I assume everyone's bona fides but I worry that assuming that these are unsecured creditors who are going to be on the steering committee

how much freedom a disbursing agent would have to start suing to recover preferences perhaps given to members of the steering committee.

So I just don't understand this whole concept of a [36] disbursing agent and steering committee at least in a case this size, and why the debtor isn't just paying the money out which is something that could have been done and saved a lot of money. Maybe I'm missing something but I'm not missing the expense that is going to be involved in consummating this plan. Now the benefits maybe I am missing. If the cases were converted substantive consolidation and all those benefits would be available. I guess there are certainly simpler mechanisms for suing people for distributing money. There is a known accountability which I find ambiguous and unclear under the debtor's plan.

There is a provision for bonding for trustees which I suppose is solvable in a plan but at least doesn't exist as it is. So, yes, there are costs too in a Chapter 7 case but I'm unconvinced at all that either the costs or delay would be any more substantial in a Chapter 7 case than they would be in a Chapter 11 case.

So I start with all that. I start – actually I start with the frankly in spite of the attempts to get around it that grounds have been shown and cause has been shown here. The estate is diminishing. There may – there may be causes of action out there which would exist in a Chapter 11 or 7 but as we sit here the administrative expenses are running. That diminishes the estate.

Rehabilitation. Everything I have read and my [37] understanding, the simple understanding of it, means a

rehabilitation of the debtor and its business. No rehabilitation is proposed here. Yes, a reorganization as that term – word is used can include a liquidation like this but rehabilitation does not encompass what the debtor is doing here so cause has been shown. The debtors are right, however, that Section 1112 says may so there is a lot of steps here.

The trustee – the U.S. Trustee has shown cause and that cause has been shown. If you are looking for a record I think it is in the debtor's own statements, it's [sic] own disclosure statement, its own affidavits and statements, so cause has been shown. The third step would be whichever is in the best interest of creditors. I guess conversion over dismissal would be if we got that far but there is the may and I'm not required just because cause has been shown.

I am willing to give the parties an opportunity – I mean that's kind of on the other side of this. I mean the people with the money on the table are all sitting on this side of the room. Nobody even wants to sit on this side of the room except – you may not have looked when you came in, Ms. Knowles, that you really belonged on that side of the room. The people with the money are over here and that doesn't count for everything but it counts for something, and I'm willing to give the parties a chance to see if they can come up with something that can convince me –

[38] I'll warn you if you haven't gotten the point it's not the plan or something that looks like it that is in the file right now. If that kind of thing with all the – with disbursing agents and committees and stuff – I mean that just sounds incredibly cumbersome and expensive to me, not to mention time consuming and delaying, but you know, if you are going to come up with a plan that is going

to pay all the unsecured creditors in full out of selling the NOL, and I don't know if that is possible either – well, I know it's possible.

Whether it can happen in this case or not I don't know but I'm surely not going to undercut and eliminate the chance for the parties to try to figure that out, and if you think you can do it in a month then, you know, more power to you.

So the bottom line is my inclination is to convert the case unless something really substantive, affirmative, that looks likely, has some likely possibility of confirming it that everybody is behind and so by the 13th of March we all come back and we are still all fighting, we are at each other's throats and we are going to sue each other and dispute who is going to be suing whom over what and having authority then this case is going into Chapter 7, but if in the meantime you can come up with some sort of consensual plan that looks like it is going to create a significant return to creditors over what they would get in a Chapter 7 case, you know, then we'll take a look at it then.

* * *

UNITED STATES BANKRUPTCY COURT
DISTRICT OF MINNESOTA
MINNEAPOLIS, MINNESOTA

In re: HEALTH RISK MANAGEMENT, Debtor.	Docket No. BKY 01-43354
HRM CLAIM MANAGEMENT, INC., Debtor.	Docket No. BKY 01-43355
INSTITUTE FOR HEALTHCARE QUALITY, INC., Debtor.	Docket No. BKY 01-43356
HEALTH BENEFIT REINSURANCE, INC., Debtor.	Docket No. BKY 01-43357 Minneapolis, Minnesota March 7, 2002 3:30 p.m.

TRANSCRIPT OF HEARING ON MOTION
FOR CONVERSION OF CASES BEFORE
THE HONORABLE ROBERT J. KRESSEL
UNITED STATES BANKRUPTCY JUDGE

Appearances:

For Debtor: JAMES BAILLIE, ESQ.
Frederickson & Byron
900 2nd Avenue South
Suite 1100
Minneapolis, MN 55402

For Unsecured Creditors Committee:	JAMES RUBENSTEIN, ESQ. Moss & Barnett 4800 Wells Fargo Center 90 South 7th Street Minneapolis, MN 55402
[2] For the U.S. Trustee:	MICHAEL FADLOVICH, ESQ. Office of the U.S. Trustee 1015 U.S. Courthouse 300 South 4th Street Minneapolis, Minnesota 55415
Court Recorder:	Kathy Barksdale U.S. Bankruptcy Court Minneapolis, Minnesota

Proceedings recorded by electronic sound recording, transcript prepared by transcription service.

* * *

[12] address some of the immediate concerns raised by the committee in its motion for expedited relief. We have no answers about the intentions. Mr. Baillie can tell us the present state of affairs in terms of who has check writing authority, but I don't believe he can assure us that the chief restructuring officer won't change that at any time. Therefore, we ask that the court grant our motion.

THE COURT: Well, the irony here is a couple weeks ago when the Debtor stood up here and said, "Oh, it's the creditors, unsecured creditors' money, so you should certainly do whatever it is the unsecured creditors committee thinks you should do." Now that the unsecured creditors committee has shifted side, the Debtors say, "No, you can't trust the unsecured creditors committee, they don't know what is in their own best interest."

But the bottom line as I sit here is I really did not see in the motion or heard today any reason to do this on such an expedited basis. There may be some concerns here, but I haven't seen any evidence to indicate that there is any urgency that would necessitate hearing this motion before we're going to be back here anyway.

So I'm going to continue the committee's motion to the same time and place as the hearing we've already scheduled on the motion of the U.S. Trustee, which is when? I heard the 13th. Does anybody know what time that is?

MR. FADLOVICH: Two o'clock, I believe.

[13] THE COURT: Is it? Okay.

So I'll continue this to the 13th at 2 o'clock.

Thanks.

(Whereupon, the hearing in the above-entitled matter was continued to be heard on March 13, 2002 at 2:00 p.m.)

UNITED STATES BANKRUPTCY COURT
DISTRICT OF MINNESOTA
MINNEAPOLIS, MINNESOTA

In re: HEALTH RISK MANAGEMENT, Debtor.	Docket No. BKY 01-43354
HRM CLAIM MANAGEMENT, INC., Debtor.	Docket No. BKY 01-43355
INSTITUTE FOR HEALTHCARE QUALITY, INC., Debtor.	Docket No. BKY 01-43356
HEALTH BENEFIT REINSURANCE, INC., Debtor.	Docket No. BKY 01-43357 Minneapolis, Minnesota March 13, 2002

TRANSCRIPT OF HEARING
ON MOTIONS TO CONVERT BEFORE
THE HONORABLE ROBERT J. KRESSEL
UNITED STATES BANKRUPTCY JUDGE

Appearances:

For Debtor: JAMES BAILLIE, ESQ.
Frederickson & Byron
900 2nd Avenue South
Suite 1100
Minneapolis, MN 55402

For Unsecured Creditors Committee:	JAMES RUBENSTEIN, ESQ. Moss & Barnett 4800 Wells Fargo Center 90 South 7th Street Minneapolis, Minnesota 55402
	[2] NANCY PETERMAN, ESQ. Greenberg & Traurig 77 West Wacker Drive Suite 2500 Chicago, IL 60607
For the U.S. Trustee:	MICHAEL FADLOVICH, ESQ. Office of the U.S. Trustee 1015 U.S. Courthouse 300 South 4th Street Minneapolis, Minnesota 55415
For Creditor, Loop Corporation and Loop Entities:	ROBERT FISHMAN, ESQ. 1144 West Fulton Street Suite 200 Chicago, Illinois 60607
Court Recorder:	Kathy Barksdale U.S. Bankruptcy Court Minneapolis, Minnesota

Proceedings recorded by electronic sound recording, transcript prepared by transcription service.

* * *

[32] So unfortunately there was just as I mentioned before an impasse in the negotiations. As for these net operating losses from the committee's perspective under the plan the beneficiary of those net operating losses under the plan is primarily Loop and again in order to have the opportunity to make use of those net operating losses Loop should contribute some consideration to the creditors.

We are here on a motion to convert which presumably was sent out to all creditors and there was no creditor that filed an objection to the motion to convert. Certainly no creditor supported it but no creditor came in affirmatively opposing this motion. The plan that is proposed is a plan proposed by the debtor. The debtor is not really even a player here in this case. The debtor is there because it has to be there but it is really the committee who is representative of the unsecured creditors who represents the true stakeholders and the committee believes that conversion is in the best interest of the estate.

THE COURT: Well, I made certain findings and determinations last time which I won't repeat that incorporate that cause has been shown to convert these cases. The estates are continuing to incur losses and it's being diminished and there is no opportunity or change for rehabilitation. The only reason I didn't convert the case last time frankly was the request by the committee for an opportunity to explore this [33] plan. The debtors's views I discounted then, I discount now. The debtor in this case is nothing more than a stakeholder. It has no interest in this money and its position really is – means almost nothing to me.

What I have here Loop's view matters. It's at least a party in interest with a possibility to the funds. I agree with Loop to a certain extent that the mere fact that the plan won't be consensual isn't cause – reason to convert the case but that's what I told people last time. The only reason I was – I gave people like five weeks to see if on a fairly expedited cheap basis people could agree on a plan. Obviously that hasn't happened. I don't really care why.

I don't really care to determine whose fault it is, if anybody's, but the fact is that the committee which seems to me is the representative body here to make the determination about what is best for unsecured creditors was unable to sign on to the Loop's plan which I guess the debtor has nominally proposed now and it has decided no. The terms of the – on which I continued the hearing have not been met and so I'm going to grant the motions and convert the cases to Chapter 7.

(Hearing concluded.)

* * *